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Executive Summary:

Changes in the OASI Benefit Distribution Under Various Social Security Reform Alternatives

- ***How Social Security benefit cuts would affect recipients by benefit level:*** This article examines changes in the distribution of Old-Age and Survivors Insurance (OASI) benefits (the primary Social Security program) resulting from various widely discussed Social Security reform alternatives. It focuses on five alternatives: Current-law benefits; gradually reducing benefits; increasing the normal retirement age; adopting “progressive price indexing,” which would affect upper-income beneficiaries more than lower-income ones; and a combination of raising the retirement age and progressive price indexing.
- ***Social Security’s role in reducing elderly poverty:*** Social Security is the primary source of income for Americans age 65 or older, and almost the only source of income for the poor elderly. Any changes to Social Security that would reduce benefits in order to eliminate future projected deficits could have a dramatic effect on the percentage of elderly living below the poverty level.
- ***Percentage with benefits below poverty:*** The percentage of beneficiaries with benefits below poverty is projected to decrease dramatically in the future due to assumed real growth in wages, which is passed along in higher benefits. Consequently, even with benefit cuts large enough to eliminate Social Security’s projected financial deficit, the percentage of beneficiaries below poverty is projected to decline.

Tax Expenditures and Employee Benefits: Estimates From the FY 2007 Budget

- ***Required by Congress:*** The president is required to provide a list of “tax expenditures” (federal tax revenue forgone due to preferential provisions) be included in the budget. The concept of “tax expenditures” has always been controversial, particularly as it counts both “tax deferred” programs (where tax revenue ultimately will be collected) and “tax exempt” ones (where no revenue will ever be collected).
- ***Benefits account for the largest share:*** For the next fiscal year (2007), all employee benefit-related tax expenditures (\$313.170 billion) will account for 37.4 percent of the \$837.068 billion tax expenditures in the budget. Tax-favored employment-based health insurance benefits will account for the largest tax expenditure presented in the budget (17.5 percent of the total) followed by employment-based retirement plans (11.0 percent of the total amount).

Changes in the OASI Benefit Distribution Under Various Social Security Reform Alternatives

by Craig Copeland, EBRI

Introduction

Social Security is the primary source of income for Americans age 65 or older: In 2004, 41 percent of all income received by those in this age group came from Social Security.¹ This share increases significantly for those age 65 or older in the lowest 25 percent of incomes (the first income quartile) and those with incomes in the next-lowest category (the second income quartile): Social Security accounted for 92 percent and 84 percent, respectively, of their income. Furthermore, as Social Security benefits have grown in real economic terms, the percentage of Americans age 65 or older whose total incomes are below the poverty level has decreased significantly, from 35.2 percent in 1959 to 9.8 percent in 2004.² Consequently, any changes to Social Security could have a dramatic effect on the percentage of elderly living below the poverty level, given their heavy reliance on this program—as shown by the significant decline in poverty over the last 40 years, during a time when Social Security benefits were virtually the *only* source of income for the lowest income elderly.

This article examines changes in the distribution of Old-Age and Survivors Insurance (OASI) benefits (the primary Social Security program) resulting from various widely discussed Social Security reform alternatives. This analysis focuses on Americans born in specific years (cohorts) whose OASI benefits commence at age 62 or older and who have not received any other Old-Age, Survivors and Disability Insurance (OASDI) benefits before that age.

The distributions of benefits presented in this study are for each *individual's* benefit, rather than for his or her family. Consequently, comparisons to the poverty thresholds in this report are biased in that more beneficiaries appear to be below each poverty threshold than would be the case when accounting for family status and the benefits of other family members. However, the changes are illustrative of the relative impacts of various reform alternatives on these benefits when compared with specific poverty thresholds.

Methodology

A representative sample of all individuals born or to be born in 1942, 1962, 1982, 2002, and 2022 is simulated using GEMINI.³ For each simulated individual, GEMINI simulates all the life events that affect an individual's Social Security benefit—including (among other factors) earnings history, marriage/divorce, job changes, death, disability, and the age when benefit receipt begins, in a manner that is representative of the current and future population based on the assumptions used that affect these life events. In combination with SSASIM, each individual simulated then has his or her OASI benefit calculated under the prescribed benefit rules for each reform examined.⁴

GEMINI and SSASIM are simulation models that, in combination, can be used to assess how the change in Social Security affects all individuals born in a year, rather than simply using stylized individuals with very specific (and unrealistic) earnings histories. Since the entire distribution of earners born in a specific year is simulated, the effect of an alternative to Social Security on the entire birth cohort can be shown against an objective standard—such as various thresholds of poverty—instead of showing the impact on a limited number of stylized individuals who are not representative of the entire population of that birth cohort.

Four alternatives to Social Security's current-law benefits are investigated in this study, each of which involves a different approach to cutting current-law benefits (see box):

- 1) A gradual reduction in benefits (GRB).
- 2) An increase in the normal retirement age (INRA).
- 3) A progressive price indexing scheme (PPI).
- 4) A combination of the progressive price indexing scheme and an increase in the normal retirement age (PPI/INRA).

Analysis Alternatives

Current Law—The benefits estimated under this alternative would be those currently scheduled under Social Security. SSASIM estimates an actuarial balance of –1.88 percent of taxable payroll under current law, slightly different from the –1.89 percent from the 2004 Board of Trustees of the Old-Age, Survivors and Disability Insurance Trust Funds Report.

Gradual Reduction in Benefits (GRB)—This change involves a decrease in currently scheduled benefits by a reduction in the primary insurance amount (PIA) factors used to calculate a beneficiary’s benefit. This reduction, which starts for those reaching the normal retirement age in 2016, would continue until those reaching the normal retirement age in 2065 have PIA factors that are 67 percent of those currently in law. This reduction would apply to all benefit types and would require an equivalent reduction each year until the cumulative reduction of 33 percent is reached in 2065. This change would eliminate the actuarial imbalance (a zero actuarial balance).

Increase the Normal Retirement Age (INRA)—Under this change, the currently scheduled increase in the normal retirement age that begins for those born in 1954 and reaches age 67 for those born in 1960 would be continued at the same rate until reaching a normal retirement age of 70 for those born in 1978. This change would improve the 75-year actuarial balance to –1.17 percent.

“Progressive” Price Indexing (PPI)—In this change a new “bendpoint” (a dollar threshold where the percent [PIA factor] of the average monthly indexed earnings [AMIE] that contributes to an individual’s primary insurance amount is changed; in 2006, the first \$656 of AMIE is multiplied by 90 percent in calculating the PIA, from \$656 to \$3,955 the PIA factor is 32 percent, and above \$3,955 the PIA factor is 15 percent) is created at 28.6 percent of the way up from the lowest bendpoint to the highest bendpoint. With three bendpoints, now there are four PIA factors. The PIA factors for the lowest two bendpoint thresholds would remain as under current law at 90 percent and 32 percent, while the factors for the higher two thresholds are price-indexed instead of wage-indexed, as is currently done. This change does not affect those with the lowest AMIEs, only those with higher earnings. This change would improve the 75-year actuarial balance to –1.08 percent.

Increase NRA and Progressive Price Index—This change would involve incorporating both the increase in the NRA described above and the progressive price indexing scheme described above. The 75-year actuarial balance would improve to –0.45 percent under this alternative.

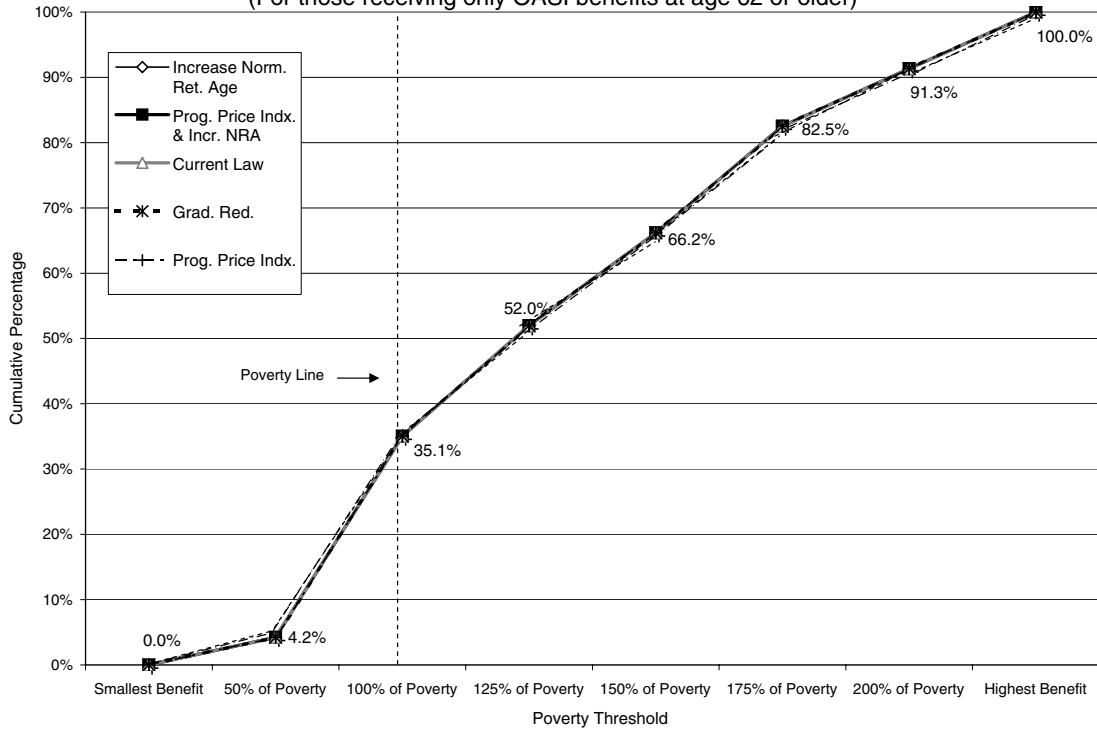
The initial-year benefits for the sample of individuals who are representative of everyone who was or will be born in the years examined are estimated in 2004 dollars. The cumulative distribution of benefits under each alternative relative to various poverty thresholds (in 2004 dollars) is then determined to see what percentage of individuals receiving only OASI benefits that commence at age 62 or older have these benefits below each of the poverty level thresholds presented. Correspondingly, the cumulative distribution also allows for the determination of the percentage of OASI beneficiaries above each threshold.^{5, 6}

Results

About to Retire (Figure 1)—The first birth cohort examined consists of those born in 1942 (64 years old in 2006). For this birth cohort, there are no differences in the percentage below each poverty threshold among the alternatives, as none of the changes under the alternatives are implemented for this cohort. However, this group provides a benchmark, as these individuals are currently just starting to receive benefits. The proportion of beneficiaries who begin receiving OASI benefits at age 62 or older who would receive a benefit below poverty would be 35.1 percent, and 91.3 percent would have a benefit below 200 percent of poverty.

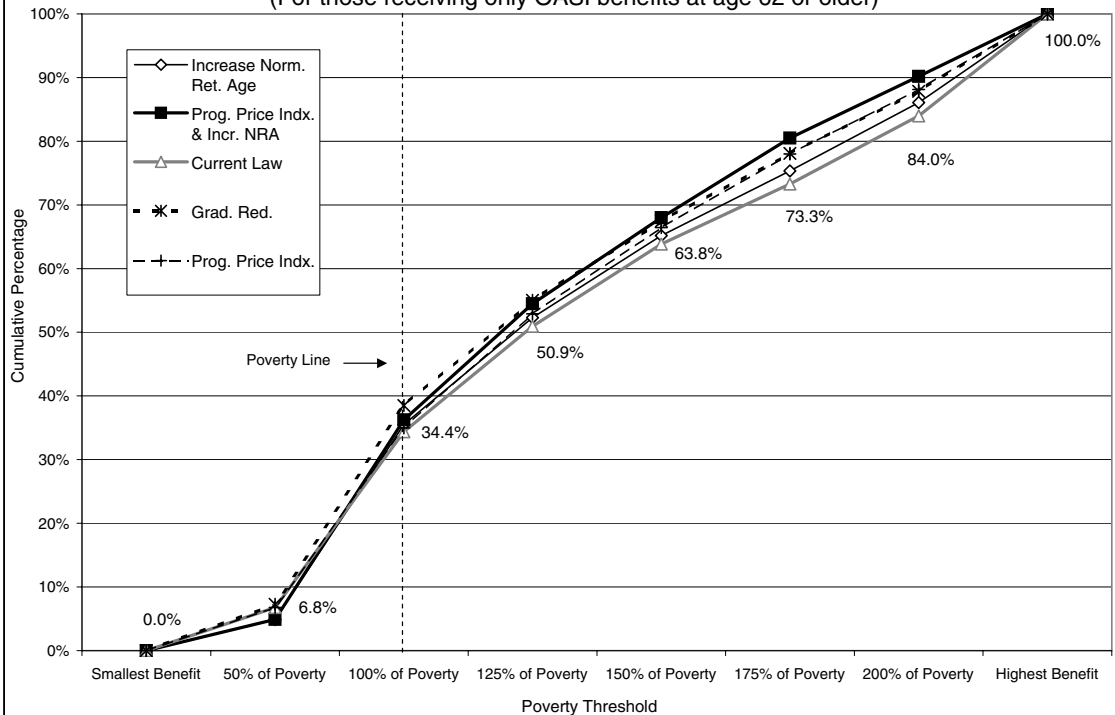
Middle-aged (Figure 2)—For those born in 1962 (44 years old in 2006), the effects of the changes from the alternatives are just beginning to show, as differences emerge in the percentage of beneficiaries receiving benefits below each threshold. For example, under current law, 34.4 percent of these recipients would have benefits below poverty, compared with 38.5 percent of the individuals under GRB. Furthermore, 73.3 percent of these beneficiaries would have benefits below 175 percent of poverty under current law, compared with 80.5 percent under PPI/INRA. This difference reflects the larger reduction in benefits from progressive price indexing for higher earning individuals relative to the proportional reduction under GRB; as a result, the reform alternatives with progressive price indexing have the highest levels of individuals below 200 percent of poverty, but lower levels below 100 percent of poverty.

Figure 1
Cumulative Distribution of OASI Benefits Relative to Poverty Thresholds
for Those Born in 1942 Under Various Social Security Alternatives
 (For those receiving only OASI benefits at age 62 or older)



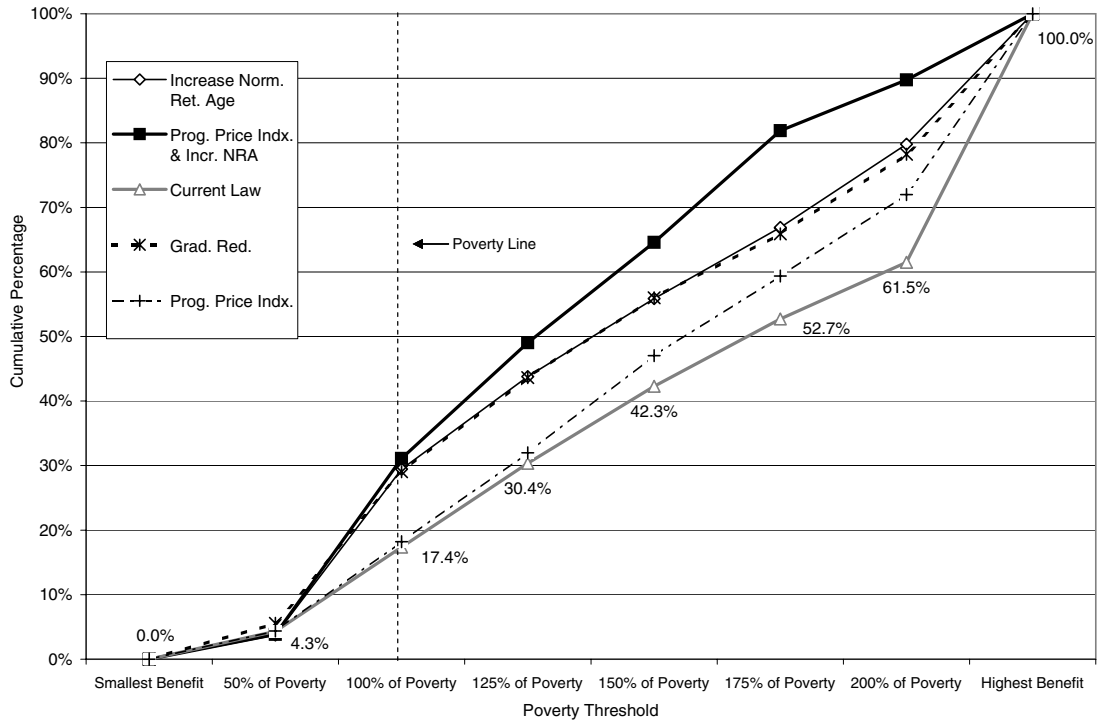
Source: Employee Benefit Research Institute analysis using GEMINI and SSASIM from the Policy Simulation Group.

Figure 2
Cumulative Percentage of OASDI Benefits Relative to Poverty Thresholds
for Those Born in 1962 Under Various Social Security Alternatives
 (For those receiving only OASI benefits at age 62 or older)



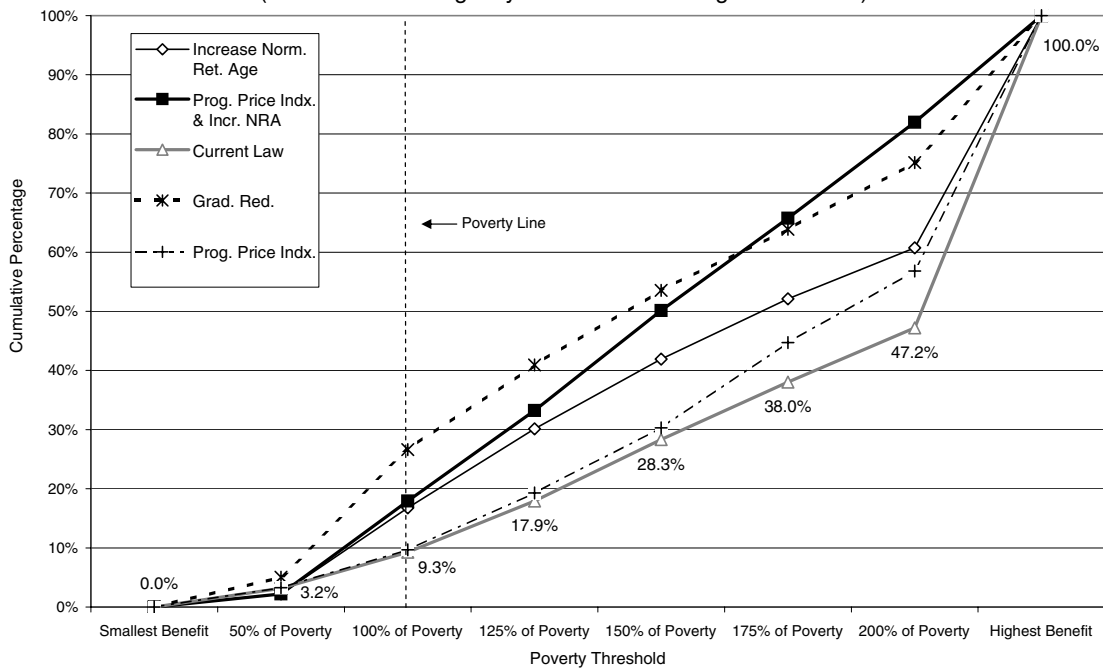
Source: Employee Benefit Research Institute analysis using GEMINI and SSASIM from the Policy Simulation Group.

Figure 3
Cumulative Percentage of OASDI Benefits Relative to Poverty Thresholds
for Those Born in 1982 Under Various Social Security Alternatives
 (For those receiving only OASI benefits at age 62 or older)



Source: Employee Benefit Research Institute analysis using GEMINI and SSASIM from the Policy Simulation Group.

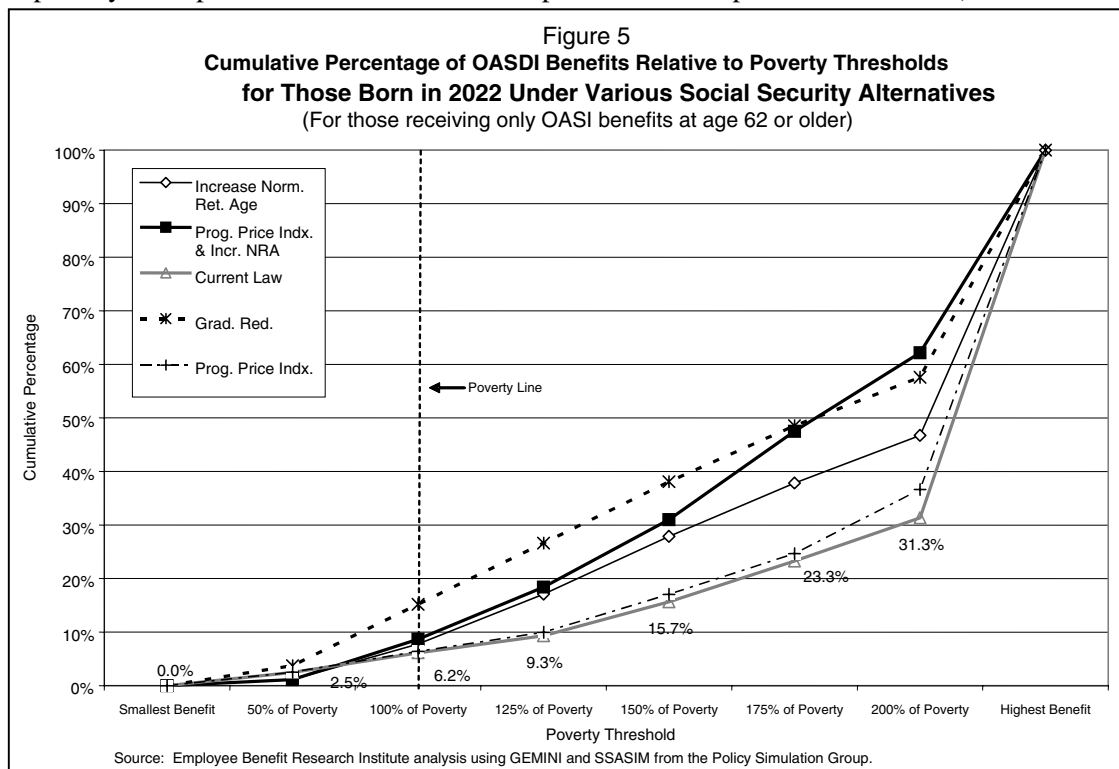
Figure 4
Cumulative Percentage of OASDI Benefits
Relative to Poverty Thresholds for Those Born in 2002
Under Various Social Security Alternatives
 (For those receiving only OASI benefits at age 62 or older)



Source: Employee Benefit Research Institute analysis using GEMINI and SSASIM from the Policy Simulation Group.

Workers Starting Out (Figure 3)—When reaching the 1982 birth cohort (24 years old in 2006), dramatic differences emerge in the percentage of recipients below each level of poverty. Under current law, only 17.4 percent of beneficiaries would have a benefit below poverty. For comparison, 31.1 percent of beneficiaries would be below poverty under the PPI/INRA alternative. This difference grows to a 29.2 percentage-point difference for those below the 175 percent of poverty threshold (52.7 percent, compared with 81.9 percent). The impact of the progressive price indexing alternative is clearly revealed in this cohort, as there is virtually no difference between this alternative and current law for individuals with a benefit below 125 percent of poverty. However, for poverty thresholds above 125 percent of poverty, the difference in benefits between the two alternatives grows until reaching 7.5 percentage points for the 200-percent-of-poverty threshold.

The Very Young (Figure 4)—For those born in 2002 (4 years old in 2006), under current law the percentage who would have a benefit below poverty would fall to 9.3 percent. For this group, the gradual reduction in benefits (GRB) changes would have reached its full cumulative effect, as 26.6 percent of recipients would receive a benefit below poverty. Furthermore, a significant difference emerges between the gradual reduction and the other alternatives, as the next-highest percentage below poverty was 17.9 percent under the PPI/INRA alternative. Again, the PPI/INRA alternative supplanted the GRB alternative in having a higher percentage with a benefit below the higher poverty thresholds (i.e., for the 200 percent of poverty, 82.0 percent under PPI/NRA, compared with 75.1 percent under GRB).



Those Not Yet Born (Figure 5)—The percentage of individuals under current law who would have a benefit below poverty would decline to 6.2 percent for those who will be born in 2022 (turning 65 in 2087) (Figure 5). The percentage with a benefit below the poverty level under the GRB alternative would also decline, but would still be significantly above the current-law level, at 15.2 percent. The percentage of beneficiaries under the PPI/INRA alternative would not exceed that of the GRB alternative until the 200-percent-of-poverty threshold. Furthermore, the PPI alternative and current law would have virtually the same percentage of beneficiaries below each poverty threshold until 200 percent of poverty, where the difference would be only 5 percentage points higher for the PPI alternative. Consequently, the impact of the PPI alternative would not fully emerge for this cohort until individuals reach a benefit level above 200 percent of poverty.

Across Birth Years—When comparing the proportion of beneficiaries with benefits below 200 percent of poverty for those born in 1942 with those born in 2022, the real growth in projected benefits

becomes quite evident. Under current-law benefits, 91.3 percent of those born in 1942 would have a benefit below 200 percent of poverty, compared with 31.3 percent for those born in 2022—a decline of two-thirds. Correspondingly, the proportion of beneficiaries under current law with a benefit greater than 200 percent of poverty would increase from about 10 percent to nearly 70 percent between the two birth cohorts. Even when comparing the gradual reduction in benefits alternative for those born in 2022 with current-law benefits for those born in 1942, the proportion who would receive a benefit below poverty would be more than 50 percent less for those born in 2022 under the GRB alternative.

Conclusion

Under current law, the proportion of OASI beneficiaries receiving benefits below poverty is projected to decline significantly for those age 24 or younger (born in 1982 or after). This is because the benefit formula currently in law passes on real wage growth earned during working years into higher benefits at retirement.

However, this projected level of real wage growth may or may not result in the future. The effect of the projected growth not being reached is illustrated by comparing the distribution of benefits for the 1942 cohort with that of the 1962 cohort, where only small changes occurred in the percentages below each poverty level. Wage growth for these cohorts was unevenly distributed and below the assumed average rate of wage growth in some years and for a significant percentage of workers for most of their working years. In contrast, large changes in the proportion of those below the poverty thresholds are seen for the 1982 cohort relative to the 1962 cohort, where most of the individuals' working years are projected using the assumed level of real wage growth instead of the actual rate as for those in the 1962 cohort. Consequently, with the projected level of real wage growth, any alternatives to current law that involve benefit cuts appear to be more palatable in relative terms, as a reduction in current law benefits of 33 percent for those born in 2022 would leave only 15.2 percent of beneficiaries born in that year with a benefit below poverty, compared with 35.1 percent for those born in 1942 under current law.

Since the real wage growth may not materialize, the cross-cohort comparisons may not match reality, but provide a relative direction on the alternatives over time. The within-cohort comparisons provide the relative scope of differences in the benefit distributions for each of the alternatives. These within cohort comparisons only show significant changes for those born in 1982 or after in their benefits relative to current law, due to the benefit cuts being phased in under the alternatives.

The most significant result of this study is that an across-the-board cut in benefits (such as those under GRB) clearly has a significantly different distributional effect than that under PPI. While the PPI/INRA alternative improves the financial soundness of the Social Security program by an amount similar to the projected elimination of the funding deficit under GRB, PPI/INRA obtains most of its savings from cuts in benefits to beneficiaries whose benefits are 125 percent or more of poverty, compared with the proportional reduction under GRB. The INRA alternative has a proportionally lower percentage below each poverty threshold as well, but not as low as the GRB alternative. However, the INRA alternative does not eliminate the projected deficit as GRB does; instead, it eliminates only about half the deficit.

Overall, even if the projected improvements in benefits relative to poverty are *not* obtained, any real growth in wages will reduce the percentage of beneficiaries below poverty. Consequently, some cuts in the projected benefits could occur while still leaving the proportion of beneficiaries with benefits below poverty at the same level or at a lower level. Furthermore, how the alternative to current-law benefits is designed will have a significant impact. For example, the PPI-style alternative does not have much effect on beneficiaries with smaller benefits, but it would force a substantially larger cut in benefits for those with higher benefits. Therefore, the political discussion is likely to be not just about cutting benefits, but also at what benefit level a cut is acceptable and what magnitude of a cut above that level is acceptable.

Endnotes

¹ Unpublished tabulations by the Employee Benefit Research Institute from the March 2005 Current Population Survey.

² See Joseph Dalaker, "Poverty in United States: 2000," *Consumer Population Reports: Consumer Income* (U.S. Department of Commerce, September 2001); available at <http://www.census.gov/prod/2001pubs/p60-214.pdf>; and U.S. Census Bureau, "Poverty Tables," *Current Population Survey, 2004 and 2005 Annual Social and Economic Supplements* available at www.census.gov/hhes/www/poverty/poverty04/tables04.html.

³ GEMINI is a dynamic microsimulation model for analyzing the lifetime implications of Social Security policies for a large representative sample of people born in the same year. It uses birth cohort samples that represent the demographic and economic characteristics of historical birth cohorts. Consequently, the sample contains the full distribution of earners across the entire spectrum of earnings histories. This study used the 12/01/2005 version of GEMINI. For more detailed information about GEMINI, see Martin Holmer, *Introductory Guide to GEMINI* (Policy Simulation Group, January 2006); available at www.polsim.com/guide2.pdf.

⁴ SSASIM is a policy simulation model that allows for altering parameters and assumptions that affect the benefits that workers will receive under the Old-Age, Survivors and Disability Insurance (OASDI) program. This includes both the parameters that determine the benefit formula and the assumptions on demographic and economic outcomes. The demographic and economic assumptions used in this study match those used in the Board of Trustees Federal Old-Age and Survivors Insurance and Disability Insurance Trust Funds, *The 2004 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Disability Insurance Trust Funds* (March 23, 2004); available at <http://www.ssa.gov/OACT/TR/TR04/>. For further information on SSASIM, see Martin Holmer, *Introductory Guide to SSASIM* (Policy Simulation Group, January 2006); available at www.polsim.com/guide.pdf.

⁵ A cumulative distribution is constructed by ordering each observation from lowest to highest, then adding up the number of observations meeting each successive criterion. For example, if there are 100 observations, each observation is ranked 1 to 100. Groupings that become larger in scale are then established, such as the number of these 100 observations less than 200, 200 up to 400, 400 up to 600, etc. Therefore, if there were 16 of the 100 observations less than 200 and 25 from 200 up to 400, the cumulative distribution would show 16 percent are less than 200 and 41 percent are less than 400. This also says that 59 percent are 400 or above. Furthermore, the percentage between two thresholds is the difference between the two percentage levels at the thresholds, so in the example, 25 percent have a value from 200 up to 400 (41 percent–16 percent).

⁶ The ratio of the initial year benefit in 2004 dollars relative to the poverty level in 2004 is the variable of interest in the cumulative distributions. The poverty level for a one-person household headed by someone who was age 65 or older was \$9,060 in 2004.

■ Tax Expenditures and Employee Benefits: Estimates From the FY 2007 Budget

by Ken McDonnell, EBRI

The federal government supports the provision of employee benefits through preferential tax treatment in the Internal Revenue Code. The Congressional Budget Act of 1974 (P.L. 93-344) requires that a list of “tax expenditures” (federal tax revenue forgone due to preferential provisions) be included in the budget. The concept of “tax expenditures” has always been controversial, particularly as it relates to programs that are “tax deferred” (such as retirement plans, under which tax revenue ultimately will be collected) rather than “tax exempt” (meaning programs in which no revenue will be ever collected) (*EBRI Issue Brief* no. 134, February 1993, provides a full review of this controversy).

For the next fiscal year (2007), all employee benefit related tax expenditures (\$313.170 billion) will account for 37.4 percent of the \$837.068 billion tax expenditures in the budget. Tax-favored employment-based health insurance benefits will account for the largest tax expenditure presented in the budget (\$146.780 billion, or 17.5 percent of the total amount and 46.9 percent of all employee benefit related tax expenditures), followed by employment-based retirement plans (\$92.270 billion, or 11.0 percent of the total amount and 29.5 percent of all employee benefit related tax expenditures). These estimates cover programs for both public-sector and private-sector programs and workers. The tax incentive is considered to be the non-taxation as *individual income* of retirement plan contributions and the value to the worker of health insurance, so the tax status of the *plan sponsor* is not relevant. As private defined benefit pensions have declined, and public defined contribution programs grown, a larger portion of the total tax expenditure each year is attributable to public-sector workers. This is also true for health benefits, as the private sector has been more aggressive than the public sector in shifting after-tax costs to workers.

The following is a listing of the employee benefits tax expenditures, as published in President Bush’s Fiscal Year 2007 budget,⁷ prepared by the White House Office of Management and Budget, using a methodology that is flawed but mandated by Congress.

Employee Benefit Tax Expenditures

	Tax Expenditures, by Fiscal Year			
	2006 ^a	2007 ^a	2011 ^a	2007–2011 ^a
	(\$ millions)			
Transportation				
Exclusion of reimbursed employee parking expenses	\$ 2,730	\$ 2,880	\$ 3,420	\$ 15,840
Exclusion for employer-provided transit passes	550	630	960	3,970
Education, Training, Employment, and Social Services				
Exclusion of employer-provided educational assistance	590	620	40	2,740
State pre-paid tuition plans	540	620	1,090	4,160
Exclusion of employer-provided child care	810	920	1,070	5,020
Employer-provided child care credit	10	10	10	80
Exclusion of employee meals and lodging (other than military)	890	930	1,110	5,080
Health				
Exclusion of employer contributions for medical insurance premiums and medical care	132,730	146,780	212,820	888,990
Self-employed medical insurance premiums	4,240	4,630	6,730	28,060
Medical Savings Accounts/Health Savings Accounts	1,830	2,650	3,860	17,890
Exclusion of Social Security Benefits				
Old-Age and Survivors Insurance benefits for retired workers	19,350	19,590	23,330	104,870
Benefits for dependents and survivors	3,980	4,040	4,360	20,750
Disability insurance benefits	3,810	4,110	5,530	23,500
Income Security				
Exclusion of railroad retirement system benefits	390	380	350	1,830
Exclusion of workers' compensation benefits	6,000	6,180	7,090	33,150
Exclusion of special benefits for disabled coal miners	50	50	40	210
Exclusion of military disability pensions	110	110	130	610
Net Exclusion of Pension Contributions and Earnings				
Employment-based plans	87,690	92,270	84,200	460,870
Employer plans	50,360	52,470	36,910	228,000
401(k) plans	37,330	39,800	47,290	232,870
Individual retirement accounts	4,230	5,970	8,060	38,350
Keogh plans	9,990	10,670	15,040	63,180
Special ESOP rules (other than investment credit)	1,760	1,890	2,490	10,910
Low and moderate income savers	1,380	830	0	830
Exclusion of Other Employee Benefits				
Premiums on group term life insurance	2,070	2,180	2,490	11,610
Premiums on accident and disability insurance	290	300	340	1,600
Income of trust to finance supplementary unemployment benefits	20	20	20	100
Veterans' Benefits and Services				
Exclusion of veterans' disability compensation and death benefits	3,600	3,770	4,350	20,210
Exclusion of veterans' pensions	140	140	150	720
Total	\$289,790	\$313,170	\$389,080	\$1,765,130
Addendum				
Deductibility of mortgage interest on owner-occupied homes	72,060	79,860	108,280	471,430

Source: White House Office of Management and Budget, *Analytical Perspectives, Budget of the United States Government, Fiscal Year 2007* (Sec. 33.6, p. 291), www.whitehouse.gov/omb/budget/fy2007/

^a Projected.

There are three types of tax treatments for employee benefits: tax exemption, tax deferral, and other preferential treatment:

- **Tax-exempt** treatment in the tax code means that the benefit is not considered taxable income to the individual. Examples of employee benefits that receive this type of tax treatment are health insurance, educational assistance, legal assistance, child-care, discounts, flexible spending accounts, parking, cafeteria facility, and meals. The largest of these is health insurance. According to the president's 2007 budget, the tax exemption for employment-based health insurance is projected to cost the federal government \$889.0 billion from 2007 through 2011. This is tax revenue the federal government will not recoup at some later point.
- **Tax-deferred** treatment means that the employee is not immediately taxed on (1) the contributions the employer and/or the employee makes to the plan, and/or (2) on the earnings on plan assets as they accumulate, but will typically be taxed on portions not previously taxed when the benefit is paid. Examples of employee benefits that receive this type of tax treatment are Keogh plans, defined benefit pension plans, defined contribution plans (such as 401(k) plans), and individual retirement accounts (IRAs). According to the president's 2007 budget, the tax exemption for employer plans is projected to cost the federal government \$460.9 billion from 2007 through 2011. When IRAs and Keoghs are added, the tax revenue loss estimate is \$562.4 billion for 2007–2011.

The revenue loss estimate for pension contributions and earnings is different from health insurance. The tax revenue loss estimate is actually a *deferral* of taxation, rather than an exemption. At some point in the future, when the individual starts drawing a benefit from the plan, the federal government will receive some tax revenue from the benefit payment.

- **Other benefits** are subject to limits and/or provisions with respect to tax treatment. For example, employer payments to the premium of life insurance are tax-exempt to the employee up to a benefit of \$50,000; any premium amount for a benefit greater than \$50,000 is taxable income to the employee. The benefit payout from a life insurance policy is not taxable income to the beneficiary. According to the president's 2007 budget, the tax exemption for employment-based life insurance is projected to cost the federal government \$11.6 billion from 2007 through 2011.

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